NADA GET THE FACTS

# FAQs

## IN-DEPTH ANSWERS ABOUT THE FRANCHISED AUTO DEALER NETWORK

**Q**

### WHY DO STATE AUTO DEALER FRANCHISE LAWS EXIST?

**Auto dealer franchise laws drive competition for new-car and new-truck sales and prevent monopoly pricing by automobile manufacturers, who otherwise could set a nationwide, non-negotiable price for a given model.**

**A**

To protect consumers, all states regulate important retail industries. This includes everything from eyewear to insurance to the automobile, which is often the second biggest purchase a consumer will make in his or her lifetime (after a home). Unlike other products, automobiles are massive purchases that require licensing and insurance to operate, usually require third party financing, and even contain some hazardous materials. Some states allow automakers to sell directly to consumers while others require local franchises to sell them. Most states agree the public is best served when multiple retailers fiercely compete for business and make the highly complex and regulated transaction easy for consumers.

Ultimately, states enact dealer franchise laws for three main reasons. First, these laws drive price competition among dealers and avoid automaker monopolies (where automakers otherwise could set inflexible, nationwide prices on their vehicles). Second, they provide an extra layer of accountability on warranty and recall issues. Finally, local ownership of automobile retailing helps local economies and creates good paying local jobs. And local dealers add value to the ownership experience well beyond the sale itself, including test-drives of multiple models of competing brands, financing, trade-ins, safety and environmental inspections, registration, tags, repairs, warranties, and safety recalls.

**Q**

### AREN'T DEALERS "MIDDLEMEN" WHO CREATE EXTRA COSTS FOR CONSUMERS?

**"Middleman costs" are a myth. The costs of retailing cars—from lots, service centers, and real estate to employees, training, and marketing—exist whether incurred by a dealer or a factory.**

**A**

Factory-direct models do not eliminate the costs of retailing or servicing a new vehicle. Factory-owned retailers require the same operating expenses and the same investment in land, buildings, and staff that franchised dealers now shoulder. In fact, franchised auto dealers' cumulative investment in land, equipment, and facilities in their local communities exceeds $200 billion (which reflects expenses that automakers would otherwise incur).

Moreover, taking dealers out of the mix wouldn't eliminate the consumers' need for a trained professional to handle trade-ins, registration and titling, and vehicle delivery, or to arrange for service and financing. So the real question is: "Who can best and most efficiently handle these costs?" Is it local franchised dealers or multinational conglomerates whose core business is manufacturing and not retailing? The clear answer is the local franchised auto dealers who have first-hand access to information about local consumers and the economic environment.

Ford and General Motors attempted operating their own dealerships and failed, confirming that factory stores neither deliver better customer service nor reduce consumer costs.

## Q WHAT VALUE DO FRANCHISED AUTO DEALERS ADD TO THE NEW-CAR BUYING PROCESS?

**Dealers do far more than simply "sell" vehicles—they provide test-drives, handle trade-ins, educate consumers about vehicle attributes and operation, complete extensive registration and titling work, perform warranty and recall repairs, and compete for service and financing business.**

**A** To fully appreciate the value of the franchised auto dealer, consider the needs and expectations of the typical car buyer. The typical new car is purchased for about $31,600, replaces an existing vehicle, and requires financing. Most consumers rely on the dealer to purchase their trade-in and to arrange financing. Most dealers have multiple financing sources and shop those sources for competitive rates. On average, financing obtained at a franchised new-car dealership is typically lower than comparable financing obtained elsewhere.

Consumers purchase new cars and trucks infrequently. Buyers often conduct careful research both online and at dealerships, and often may be anxious about choosing the wrong vehicle or taking on a large financial commitment. Franchised auto dealers provide car buyers with the ability to:

- Educate themselves about the cars they are considering.
- Find competitive financing consistent with their budget and credit standing (on average, dealer financing is typically lower than bank financing).
- Sell their trade-in vehicles into a ready market for used cars and trucks.
- Obtain worry-free registration and titling services.
- Have immediate access to inventory, routine maintenance and warranty or recall repairs.

Thanks to the franchised auto dealer, consumers have easy access to the manufacturer's suggested retail price (MSRP) and the invoice prices paid by dealers. Consumers can browse inventory, engage multiple dealers in price discussions, and learn about manufacturer incentives online, by phone, or by visiting dealerships. To put the system in context, can you imagine going to Wal-Mart, learning exactly how much Wal-Mart paid for a flat screen TV, and then being able to negotiate and cross-shop other TV retailers to drive the price of that exact model down further? That's the benefit dealers currently deliver to consumers.

## Q DON'T FRANCHISE LAWS LIMIT COMPETITION?

**State laws do not give existing dealers the unilateral right to block the addition of new dealers. Rather, state laws typically give existing dealers the ability to challenge as economically unjustified the proposed addition of a new dealer in the existing dealer's immediate neighborhood. But, for the dealer to prevail, the new outlet must be shown to, in fact, be unjustified. These rights are appropriate given the enormous, multi-million dollar financial commitment dealers invest in their communities to build and run their dealerships. And, in any event, consumers can still easily shop at the same brand dealers in nearby markets.**

**A** Although no states give existing dealers the absolute power to block the addition of new dealers, state franchise laws typically give existing dealers the ability to challenge as economically unjustified the proposed addition of a new dealer in the existing dealer's immediate neighborhood. But, for the dealer to prevail, the new outlet must be shown to, in fact, be unjustified. These rights are appropriate given the enormous, multi-million dollar financial investment dealers make in the local economy for facilities, vehicle purchases, equipment, personnel (good, local jobs) marketing, and training—all of which is necessary to serve consumers. But even then, there is real competition among same brand dealers in a given geographic area. For example, in a 10-mile radius in northern Virginia, consumers can purchase Ford cars and trucks from no less than five competing dealers.

Prior to state franchise laws, it was a one-sided deal in favor of national or international manufacturers who could strip a dealer of his or her private investment on a whim. State lawmakers across the U.S. created these laws to level the playing field and ultimately serve the best interests of the public. Even the U.S. Supreme Court backed dealer franchise laws in a landmark ruling stating that weakening these laws, "…would be injurious to the existing franchisees and to the public interest."

## Q
### DON'T DEALERS HAVE THEIR OWN MONOPOLY ON THE SALE OF NEW CARS?

**There are more than 17,500 franchised new-car dealers across the U.S., each fiercely competing locally against each other (both inside their own brand and with dealers of other brands) for customer business on price and service. That is about the opposite of a monopoly.**

**A** To say that franchised new-car dealers have a monopoly on the sale of new cars is like saying that doctors have a monopoly on the practice of medicine. There are more than 17,500 franchised new-car dealers across the U.S., each fiercely competing locally against each other (both inside their own brand and with dealers of other brands) for customer business on price and service. What's more, not all the states address the market in the same way. Although all the states have licensing, zoning, consumer protection, and franchise laws governing the business operations and practices of new-car dealerships, no two states have the same laws because one size doesn't fit all. A monopoly would exist if factories owned all of the other dealerships and set prices.

## Q
### CONSUMERS BUY OTHER PRODUCTS LIKE COMPUTERS DIRECTLY FROM MANUFACTURERS, SO WHY NOT CARS?

**A car or truck is one of the two biggest purchases a consumer will ever make, requires complicated registration and financing, and unlike computers, can't be boxed up and sent back to the manufacturer for service, warranty, and safety recall repairs.**

**A** Automobiles are not everyday purchases. A new car or truck is the second biggest purchase the typical consumer will ever make (after a house). Cars require licenses and insurance to operate, contain hazardous materials, require many government forms to register, and often involve financing and a trade-in. Before a consumer pays upwards of $31,600 for a new vehicle, states require that the seller of that vehicle be able to service and repair that vehicle. In addition, car and truck buyers usually want hands-on test-drives with vehicles before purchasing.

When most products like computers need servicing or repairs, the consumer boxes it up, mails it to the manufacturer and waits weeks or months—without access to the product—until it is repaired and returned. That's not feasible or desirable when a financed product that is often essential to one's daily existence requires service, repairs or a safety recall.

## Q
### WHY CAN'T PEOPLE BUY NEW CARS AND TRUCKS ONLINE?

**They can, and they do so all the time. Dealers embrace the Internet: they offer consumers a wealth of specific vehicle information online, and they sell vehicles online if the consumer wants to proceed that way. However, most consumers still prefer to do the sale in-person since Internet transactions do not allow for test-drives, hands-on vehicle education, and other "tire kicking" interactions.**

**A** People buy cars and trucks online every day—from dealers! Any consumer who wants to buy online can just go to his or her dealer's website and begin the transaction. Even apart from completing the actual sales, the Internet plays a crucial role in most new car and truck purchases. That's in large part because dealers embrace the Internet by providing a wealth of specific vehicle information product specs, options, pricing, and dealer costs online. Franchised dealers have established their own websites, participate in lead generation services, and often employ specialists dedicated to answering both vehicle- and price-related questions online. Use of the Internet greatly expands the market area of each dealer, thereby greatly increasing dealer-to-dealer competition. There are no other retailers whose businesses have so completely integrated both the online and real-world experience.

Nonetheless, most consumers still prefer to complete their vehicle purchases in-person since Internet transactions do not allow for test-drives, hands-on vehicle education, or other "tire kicking" interactions. According to the Harvard Business Review, most car and truck buyers value a combination of online information, personal service, and physical locations in their local communities over stand-alone Internet sales. That's because consumers benefit from their personal relationship with the dealer who sells them a new car or truck. This is very different from trying to communicate or otherwise receive accountable customer service from a website (or toll-free operator/sales representative) located hundreds, if not thousands, of miles away.

Q

## AREN'T FACTORIES BETTER POSITIONED TO MARKET "ADVANCED TECHNOLOGY" VEHICLES AND CATER TO MORE UNIQUE CUSTOMERS?

**Dealers market and sell a wide variety of products and technologies—and they do it very well. As one example, more electric vehicles are sold through dealerships than by any other means. Moreover, automakers can establish their own criteria with dealers to reflect each brand's uniqueness—down to the uniforms worn by sales staff, special training for personnel, and how the vehicles are displayed. And manufacturers are not required to select as dealers people who serve as dealers for other manufacturers.**

A

Dealers are on the forefront of selling cars with advanced technologies. In 2013, franchised new-car dealers sold the lion's share of the country's pure electric vehicles (EVs) and virtually all of the country's plug-in electric and hybrid electric vehicles. (The number of EVs sold last year more than doubled to approximately 47,600 units but still represents only .03% of the overall U.S. vehicle market.) Of the EVs sold last year, nearly 29,000 were sold by franchised new-car dealers (60.5% of the market), including vehicles such as: the Nissan Leaf; MZB Smart; Fiat 500e; Scion iQEV; Chevy Spark EV; Ford Focus EV; Mitsubishi i-MiEV; Honda Fit EV; and Toyota RAV4 EV. In addition, franchised new-car dealers sold nearly 49,000 plug-in electric vehicles and 490,000 hybrid electric vehicles. Tesla sold approximately 18,900 Model S units in the U.S. last year and no plug-ins or hybrid electric vehicles. Tesla has suggested that, as its sales rise, it may well consider franchise dealerships.

The notion that an automaker must own its sales outlets to ensure that its products are appropriately marketed is proven false in the marketplace today. Every automaker establishes specific standards for how its cars are marketed and serviced. Franchise agreements define the design of all branding elements—including uniforms worn by the sales and service staffs, special training for sales and service personnel, and even required perks for service customers. And manufacturers do not have to select dealers who sell other cars. So, for example, if an EV manufacturer is concerned that dealers of gas powered vehicles won't represent the EV brand well, that manufacturer can simply skip over those existing dealers in deciding who to appoint to represent it in the marketplace.

Since the late 1980s, there have been at least 10 examples of new franchise networks that made varying demands on franchisees. These include Fiat, Hummer, Infiniti, Lexus, MINI, Saturn, Smart, Fisker, Scion and Coda. Franchises were awarded by the automaker to experienced dealers as well as newcomers to the business. Each of these brands and/or manufacturers set its own criteria for how it wanted its vehicles displayed, marketed, and serviced.

Q

## WOULDN'T CONSUMERS PREFER TO BUY DIRECTLY FROM AN AUTOMAKER INSTEAD OF DEALERS?

**A survey by Cars.com finds—on average—that consumers rate their dealer experience a 4.5 out of a possible 5. And when Ford and General Motors attempted to sell direct in the past, they failed in part because they did not offer better customer service.**

A

In the end, consumers actually like purchasing from local dealers. According to J.D. Power, customer satisfaction with dealers is currently at the highest point since it began measuring perceptions of dealers. And Cars.com, a leading auto industry website listing new and used car inventories, analyzed sales data and discovered that all dealers, especially franchised dealerships, get high marks from consumers, with the average dealer review earning a 4.5 out of a possible 5-point rating. In contrast, both Ford and GM failed when they experimented with direct sales. In those instances, it became clear they could not deliver on localized customer service expectations.

Consumers win in the ultra-competitive franchise system because they have so many choices. They decide what to buy and from whom, whether it's a new vehicle, service, or repair. Dealers must satisfy the customer or risk losing that business to a better competitor. In contrast, imagine a system where a national or global corporation residing far away from a consumer's hometown serves as the point of sale for the large and complex purchase of a new car or truck. Now imagine trying to get personal and speedy service—much less negotiate pricing—with a distant, faceless corporate auto sales representative. Local dealers are locally accountable with a face-to-face transaction and a hand shake.

Franchised auto dealers employ nearly 1 million people across all 50 states and the District of Columbia, and these good jobs can't be shipped overseas. These dealers are among the very last of Main Street, family-owned businesses, are actively engaged in their communities, and serve as the backbone of their local economies.